

Internal Revenue Service
memorandum

CC:TL-N-7652-87

Brl:HFRogers

date: JUN 24 1987

to: Assistant District Counsel, Dallas CC:DAL

from: Director, Tax Litigation Division CC:TL

subject:

Dkt. No. [REDACTED]

This is in response to your request for technical advice dated May 15, 1987.

ISSUE

Whether to pay the \$ [REDACTED] in costs and fees requested by the petitioners pursuant to I.R.C. § 7430. 7430.00-00

CONCLUSION

We concur in your settlement proposal. Given the facts in the instant case and the administrative errors involved, recent court opinions clearly indicate that we would be held liable for the petitioners' reasonable court costs pursuant to section 7430.

FACTS

The subject case involves the disallowance of petitioners' claimed loss from [REDACTED], a small business corporation, for the taxable year [REDACTED]. The corporation had been audited as to its [REDACTED] taxable year. The RAR issued in [REDACTED] determined that various start-up costs claimed by the corporation should be disallowed or capitalized. The corporation's [REDACTED] year was never examined.

During [REDACTED] the petitioners signed a consent to extend the statute of limitations until [REDACTED]. During [REDACTED], the Service solicited new consents from the petitioners, using an address that was no longer current. The petitioners did not respond. On [REDACTED], a notice of deficiency was sent to the petitioners' correct address.

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The petitioners' representatives responded with a letter dated [REDACTED], explaining that the corporation was never notified of any plans to examine its [REDACTED] return, offering to re-extend the statute, and asking why the notice of deficiency was issued. The Service never responded. Over two months later, a petition was filed in the subject case asserting the correctness of the return. The Service denied its allegations. District Counsel tried unsuccessfully to locate the RAR for [REDACTED], then forwarded the case to Appeals. The Appeals Officer, in [REDACTED] of [REDACTED], determined the corporation was never examined for [REDACTED], and that the notice had been issued in error. The parties then settled the case.

DISCUSSION

Section 7430 authorizes the award of reasonable litigation costs to taxpayers in certain circumstances. Under section 7430, in order to be entitled to an award of litigation costs, the taxpayer must:

- (1) substantially prevail in the litigation (section 7430(c)(2)(A)(ii));
- (2) establish that respondent's position is not substantially justified (section 7430(c)(2)(A)(i)); and
- (3) have exhausted the administrative remedies available to that taxpayer in the Internal Revenue Service (section 7430(b)(2)).

See Minahan v. Commissioner, 88 T.C. No. 23 (March 3, 1987).

1. Substantially Prevail

In the instant case, the taxpayers have substantially prevailed. Prevailing as to the most significant issue and prevailing as to the amount in controversy are alternative grounds for concluding the taxpayer has substantially prevailed. See Phillips v. Commissioner, 86 T.C. No. 26 (March 5, 1987). After making an inquiry, the Appeals Officer verified that the corporation was not under examination at all for 1980, and there were no grounds for issuing the notice of deficiency. The taxpayers prevailed as to both the issue and the amount so they satisfied the requirements of section 7430(c)(2)(A)(ii).

2. Substantial Justification

Given the facts in the instant case, the court is likely to conclude that the taxpayers have established that the Service's position is not substantially justified. Numerous unreported opinions have held that the Service is not substantially justified when it takes too long to correct its errors after the suit is filed. See, e.g., Hanes v. United States, No. 84-2626 (9th Cir. 1984); Offut v. United States, (E. D. Va. 1985); Shawver v. United States, (N.D. Iowa 1985). In the instant case, it took more than one and one half years from the time the petition was filed to ascertain that the corporation had not been under examination for [REDACTED]. This is an unreasonable length of time for such a simple issue, especially when the Service's own records were all that needed to be examined.

3. Exhaustion of Administrative Remedies

The petitioners in this subject case are deemed to have exhausted all administrative remedies available to them within the Internal Revenue Service. They were unable to consent to extend the statute of limitations (although their letter indicated they would willingly do so) because the request for an extension was sent to an address which was no longer current. Because the statute of limitations had not been extended, the Service issued a notice of deficiency (to the correct address) disallowing the claimed loss. No 30-day letter was sent so the taxpayers were unable to choose to participate in an Appeals office conference. See Treas. Reg. § 301.7430-1(f)(2).

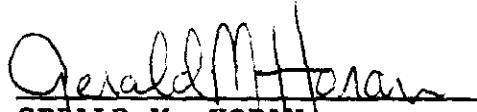
CONCLUSION

We concur in your decision to settle this issue and pay the \$ [REDACTED] in costs and fees incurred by these taxpayers. These taxpayers are entitled to an award of litigation costs pursuant to section 7430.

If you have any further questions, please contact Helen F. Rogers of this office at 566-3521.

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By:


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